

Before the  
Illinois Commerce Commission

In the Matter of  
  
Approval of an Increase and  
Adjustment of Rates and Charges for  
Water Utility Service Sold by  
**Cherry Hill Water Company** within  
Will County

Direct Testimony of

Amanda M. Ross  
Senior Regulatory Accountant

for

Cherry Hill Water Company

April 30, 2003

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1 **Q. Please state your name and business address.**

2 A. My name is Amanda M. Ross. My business address is 2335 Sanders Road,  
3 Northbrook, Illinois 60062.

4  
5 **Q. What is your occupation?**

6 A. I am the Senior Accountant for the Regulatory Department of Utilities, Inc. and its  
7 subsidiaries.

8  
9 **Q. Please summarize your professional background?**

10 A. I have been employed by Utilities, Inc. since April of 2002. Since that time I have  
11 been involved in many phases of rate-making in several regulatory jurisdictions. I  
12 graduated from Purdue University in 2000, and I am a Certified Public Accountant.  
13 I had two years of public accounting/financial analysis experience prior to joining  
14 Utilities, Inc., and I am a member of the American Institute of Certified Public  
15 Accountants.

16  
17 **Q. Please explain your job responsibilities with Utilities, Inc.?**

18 A. My responsibilities include: financial analysis of individual subsidiaries of Utilities,  
19 Inc., preparation of applications for rate relief, facilitation of commission audits,  
20 and the submission of financial testimony and schedules to support a request for  
21 an increase in rates.

22  
23 **Background**

24  
25 **Q. Please describe Cherry Hill Water Company.**

26 A. Cherry Hill Water Company is a wholly owned subsidiary of Utilities, Inc. (UI).  
27 Water Service Corporation (WSC) manages the operation for all of UI's water and  
28 wastewater systems, including Cherry Hill. WSC provides management,  
29 administration, engineering, accounting, billing, data processing, and regulatory  
30 services for the utility systems. WSC's expenses are assigned directly to a utility or  
31 distributed to the various companies pursuant to a formula that has been approved  
32 by the Commission.

1 Cherry Hill provides water usage service to approximately 236 customers in Will  
2 County. Cherry Hill's current rate structure was approved pursuant to Order No.  
3 94-0368 dated July 6, 1995.

4  
5 **Q. Ms. Ross, what is the purpose of your testimony here today?**

6 A. The purpose of my testimony is to explain to the Commission why Cherry Hill  
7 Water Company has requested an increase in water rates. I will also discuss some  
8 of the factors that have contributed to the need for the increase and the impact of  
9 the increase on our customers. I will present and describe schedules showing the  
10 overall cost of capital and proper rate of return on rate base, and I will also sponsor  
11 the Utility's financial exhibits.

12  
13 In addition, I will provide information to support Cherry Hill Water Company's  
14 request to change depreciation rates from composite rates to class-of-asset rates, to  
15 convert the current quarterly billing cycle to a monthly billing cycle, and to update  
16 the Rules, Regulations, and Conditions of Service tariffs.

17  
18 **Rate Relief**

19  
20 **Q. Why is Cherry Hill Water Company requesting rate relief at this time?**

21 A. A rate increase is necessary to allow the Utility to recover the reasonable and  
22 prudent costs of providing service and an opportunity to earn a fair and reasonable  
23 rate of return on its invested capital. Rates granted in 1995 do not reflect 8 years  
24 of rising costs, many of which result from stringent federal environmental  
25 regulations, increased investment, and inflation. For these reasons the Utility is  
26 not able to achieve a reasonable rate of return on its investment. Rate relief is  
27 essential to ensure the continued availability of capital at a reasonable cost and to  
28 maintain a high and professional level of service. Under the present rate schedule,  
29 Cherry Hill is not earning a fair and reasonable return on its investment. After  
30 making pro forma adjustments to the December 2002 test year for known, fixed  
31 and measurable changes Cherry Hill Water Company has an overall return of  
32 4.83%. The proposed rates will allow the company to earn a 9.39% overall rate of  
33 return. This information is supported in the financial statements attached hereto  
34 as **Utility Exhibit One.**

MAY 17 1995

1 **Q. Ms. Ross, what factors, or changes in the cost of service, can you point to**  
2 **that have contributed to the need for the requested increase?**

3 A. The age of the system is a factor in the cost of maintenance to be done. As the  
4 system ages, the cost of maintenance increases. Cherry Hill Water Company is  
5 committed to maintaining clean, safe, professional facilities. Our facilities are  
6 visible throughout the communities we serve.

7

8 **Rate Analysis**  
9

10 **Q. What are the present water rates for Cherry Hill Water Company and when did**  
11 **they become effective?**

12 A. The present usage rates became effective on July 6, 1995, and are as follows:

13

14 Base Facility Charges:

15 Residential:

16 5/8" Meter \$18.00

17 2" Mobile Home Pk \$51.45

18 Gallage Charges: \$4.24 per 1,000 gallons

19

20 It should be noted that these rates are billed quarterly. The current quarterly  
21 average consumption for residential customers in Cherry Hill is approximately  
22 16,342 gallons. This equates to a quarterly bill of \$87.29.

23

24 **Q. What are the proposed water rates for Cherry Hill Water Company and their**  
25 **impact on the average customer?**

26 A. The proposed rates are as follows:

27

28 Base Facility Charges:

29 Residential:

30 5/8" Meter \$7.75

31 2" Mobile Home PK \$22.50

32 Gallage Charges: \$4.74 per 1,000 gallons

33

34 These rates will be billed monthly pending the Commission's approval of the  
35 Company's request to convert the current quarterly billing cycle to a monthly

END OF TEST

1 billing cycle. Based on an average consumption of 5,464 gallons per month, the  
2 customers' monthly bill will be \$33.34 or an increase of \$4.54 per month.

3  
4 **Cost of Capital**

5  
6 **9. What is the cost of capital of Cherry Hill Water Company?**

7 A. The cost of capital of Cherry Hill Water Company is determined by using UI's  
8 capital structure. These cost of capital percentages are then used to ascertain the  
9 overall cost of capital for Cherry Hill Water Company. The capital structure and  
10 cost rates that I proposed to use in this proceeding are as follows:

11

	<u>Weight</u>	<u>Cost</u>	<u>Weighted Cost</u>
Debt	45.69%	8.64%	3.95%
Equity	<u>54.31%</u>	<u>10.02%</u>	<u>5.44%</u>
Overall	<u>100.0%</u>		<u>9.39%</u>

12

13 **9. Why must one determine the overall cost of capital for a public utility?**

14 A. The proper balance of rate payer and shareholder interest occurs when the  
15 Commission authorizes a public utility a rate of return on its rate base equal to its  
16 overall cost of capital. If the authorized rate of return on rate base exceeds the  
17 overall cost of capital, then rate payers bear the burden of excessive prices.  
18 Conversely, if the authorized rate of return on rate base is lower than the overall  
19 cost of capital, then the Utility will be unable to raise capital at a reasonable cost.  
20 Ultimately, the Utility may be unable to raise sufficient capital to meet demands for  
21 service, thereby impairing service quality. Therefore, ratepayers interest are served  
22 best when the authorized rate of return on rate base is neither higher nor lower  
23 that the overall cost of capital.

24

25 **9. Please define "overall cost of capital"?**

26 A. The overall cost of capital equals the sum of the costs of the components of the  
27 capital structure (debt and common equity) after each is weighted by its proportion  
28 to total capital.

29

30

31

1   **Q.   How does Cherry Hill raise capital?**

2   A.   Capital for Cherry Hill is raised by Utilities, Inc. Cherry Hill Water Company is a  
3       wholly owned subsidiary of Utilities, Inc. The source of this capital is banks and  
4       large lending institutions  
5

6   **Q.   How did you determine the cost of debt to Cherry Hill?**

7   A.   The 8.64% cost of debt is the embedded cost of debt of the Utilities, Inc., the parent  
8       company of Cherry Hill, as of December 31, 2002. This percentage is consistent  
9       with past Illinois Commerce Commission practice.  
10

11   **Q.   How did you derive the cost of equity used in your calculation?**

12   A.   Today's embedded cost of debt of the consolidated group is approximately 8.64%.  
13       The equity investor is entitled to a premium over the return to the debt holder  
14       because of the additional risk he or she takes. The debt holder has first claim on  
15       the assets and earnings of the Utility. These claims must be satisfied before funds  
16       are available to the equity shareholder. Therefore, the return on equity must be  
17       greater than 8.64%.  
18

19       In addition, a risk free investment, thirty-year treasury bonds, currently yields  
20       approximately 4.94%, as of April 15, 2003. Utility bonds available to investors are  
21       a higher risk than government bonds. Also available to investors are equity  
22       securities of large companies. These are publicly traded securities paying  
23       dividends and having the advantage of liquidity. Naturally, the market would favor  
24       any of these securities over the equity in a small company with non-traded  
25       securities, such as Cherry Hill. It would be reasonable to add a premium to the  
26       cost of 30-year treasury bonds to determine the cost of equity to Cherry Hill.  
27

28       In addition, in the last rate proceeding (Docket #02-0592), Staff witness Rochelle  
29       Phipps opined that 10.02% is a reasonable cost of equity for one of UI's operating  
30       subsidiaries. In view of the proceeding information, I believe that 10.02% is the  
31       minimum cost of equity and that an overall return of 9.39% is reasonable.  
32  
33  
34  
35

1     Depreciation

2

3     **Q.   What is the current method of calculating depreciation expense at Cherry Hill**  
4     **Water Company?**

5     A.   Currently, Cherry Hill Water Company multiplies all plant-in-service accounts by a  
6     composite rate of 1.50% to calculate annual depreciation expense.

7

8     **Q.   What method of calculating depreciation expense is the Utility proposing?**

9     A.   The Utility is proposing a change from using a composite rate of 1.50% to utilizing  
10    separate depreciation rates for each primary account. These rates range from  
11    1.89% to 7.69%. This method of calculating depreciation expense is consistent  
12    with prior rate proceedings approved by the Commission, including Docket No. 01-  
13    0663, Lake Wildwood Water Company, and Docket No. 02-0592, Del-Mar Water  
14    Company.

15

16    **Q.   Why is Cherry Hill Water Company proposing this change in depreciation**  
17    **rates in order to calculate depreciation expense in this rate proceeding?**

18    A.   The Utility has proposed these modified depreciation rates based on testimony filed  
19    by Staff witness King in Docket Nos. 01-0663 and 02-0592. According to this  
20    testimony, separate depreciation rates for primary accounts are more sensitive to  
21    the service life and retirement in a specific account than a composite rate. As  
22    such, rates by primary accounts result in a more accurate allocation and recovery  
23    of depreciation expense. Therefore, the Utility's calculation of depreciation expense  
24    was prepared using the average service lives, salvage values, and calculations  
25    utilized in ICC Staff Exhibit 6.00, Schedules 6.01 and 6.02 for Docket No. 01-0663  
26    and ICC Staff Exhibit 4.00, Schedule 4.04, pages 1 and 2 for Docket No. 02-0592.

27

28    **Q.   How do the depreciation rates proposed by the Utility compare to the rates**  
29    **approved by the Commission in prior rate proceedings?**

30    A.   The depreciation rates proposed by the Utility are consistent with the average  
31    service lives, salvage values, and calculations that were approved for Consumers  
32    Illinois Water Company, Northern Illinois Water Corporation, Illinois-American  
33    Water Company, Lake Wildwood Water Company, and Del-Mar Water Company.

34

1 **Q. What is the effect on Cherry Hill Water Company's depreciation expense using**  
2 **the proposed depreciation rates?**

3 A. Depreciation expense of Cherry Hill Water Company will increase by approximately  
4 \$2,623 based on proposed depreciation rates. In addition, the overall composite  
5 depreciation rates will raise from 1.55% to 2.99%. This increase is consistent with  
6 prior rate proceedings approved by the Commission.  
7

8 **Billing Cycles**  
9

10 **Q. What is the current billing schedule for the customers of Cherry Hill Water**  
11 **Company?**

12 A. Cherry Hill customers are currently billed at the end of each quarter.  
13

14 **Q. What billing schedule is the Utility proposing?**

15 A. The Utility is proposing a change from a quarterly billing cycle to a monthly billing  
16 cycle.  
17

18 **Q. Why is the Utility proposing a monthly billing cycle?**

19 A. The Utility believes that a monthly billing cycle will enable the Utility to provide  
20 better service to the customers of Cherry Hill. First, a monthly billing cycle will  
21 permit Cherry Hill customers to properly budget for water utility expenses each  
22 month. Second, customer service representatives will be able to appropriately  
23 address customer concerns as issues can be promptly detected. Third, the Utility  
24 will be able to locate and resolve system problems as customer billing and  
25 consumption data will be available monthly as opposed to quarterly.  
26

27 **Q. Is this change in billing cycles consistent with the Utility's focus on providing**  
28 **quality service to its customers?**

29 A. Yes, it is. The Utility believes that this change is beneficial to the customers and  
30 the quality of their service.  
31

32 **Q. What impact will this change in billing cycles have on operating expenses?**

33 A. The change to a monthly billing cycle will increase office expenses due to an  
34 increase in postage, bank charges, and office stock, such as paper and envelopes,  
35 which results from additional mailings and deposits made throughout the year.



1 There will also be increased meter reading expenses; however, no additional  
2 employees are required to handle the increased number of billings.  
3

4 **Rules, Regulations, and Conditions of Service Tariffs**  
5

6 **Q. Does the Utility plan to update the Rules, Regulations, and Conditions of**  
7 **Service tariffs for Cherry Hill Water Company?**

8 A. Yes, it does.  
9

10 **Q. Please explain why the Utility is proposing to update Cherry Hill's Rules,**  
11 **Regulations, and Conditions of Service tariffs.**

12 A. The Utility has proposed to update its Rules, Regulations, and Conditions of  
13 Service tariffs as they have not been updated in more than 8 years. Since this  
14 time, Staff has compiled updated Rules, Regulations, and Conditions of Service  
15 tariffs that have been provided to other Illinois regulated utilities, including  
16 Utilities, Inc., Cherry Hill's parent company. Utilities, Inc. has filed updated Rules,  
17 Regulations, and Conditions of Service tariffs for Docket No. 01-0050, Westlake  
18 Utility, Inc. and has agreed to file these tariffs for Docket No. 02-0592, Del-Mar  
19 Water Company.  
20

21 **Filing Procedures**  
22

23 **Q. Why is Cherry Hill Water Company filing under the Standard Rate Case**  
24 **Procedures instead of the Short Form Procedures that are in place for a**  
25 **company the size of Cherry Hill Water Company?**

26 A. Utilities, Inc. has determined that our short form filings are conducted in the same  
27 manner as a general rate filing. This is because Utilities, Inc. has a staff of  
28 accounting and ratemaking professionals. Additionally, under the short form  
29 process there is no formal procedure for seeking a mediation of disputed  
30 adjustments made by the Staff to the Utility's revenue requirement. This can be  
31 unfair to the Utility.  
32

33 **Q. Does this conclude your testimony?**

34 A. Yes it does.